

Members

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Sen. Richard Bray
Sen. James Merritt
Sen. Timothy Lanane
Sen. Earline Rogers
Sen. Vi Simpson
Rep. Trent VanHaaften, Vice-Chairperson
Rep. Scott Pelath
Rep. Phil GiaQuinta
Rep. Matt Bell
Rep. Jack Lutz
Rep. Thomas Dermody



INTERIM STUDY COMMITTEE ON ALCOHOLIC BEVERAGES

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Authority: P.L. 94-2008 (HEA 1118-2008)

MEETING MINUTES¹

Meeting Date: October 15, 2008
Meeting Time: 1:00 P.M.
Meeting Place: State House, 200 W. Washington
St., Room 431
Meeting City: Indianapolis, Indiana
Meeting Number: 3

Members Present: Sen. Ron Alting, Chairperson; Sen. Richard Bray; Sen. James Merritt; Sen. Timothy Lanane; Sen. Vi Simpson; Rep. Trent VanHaaften, Vice-Chairperson; Rep. Scott Pelath; Rep. Matt Bell; Rep. Jack Lutz; Rep. Thomas Dermody.

Members Absent: Sen. Earline Rogers; Rep. Phil GiaQuinta.

1. Call to order/introduction of members

Sen. Alting called the meeting to order at 1:05 p.m. Committee members and staff introduced themselves.

¹ Exhibits and other materials referenced in these minutes can be inspected and copied in the Legislative Information Center in Room 230 of the State House in Indianapolis, Indiana. Requests for copies may be mailed to the Legislative Information Center, Legislative Services Agency, 200 West Washington Street, Indianapolis, IN 46204-2789. A fee of \$0.15 per page and mailing costs will be charged for copies. These minutes are also available on the Internet at the General Assembly homepage. The URL address of the General Assembly homepage is <http://www.in.gov/legislative/>. No fee is charged for viewing, downloading, or printing minutes from the Internet.

2. Testimony and discussion

Considerations in determining the value of restaurant permits

Jeffrey McKean, McKean Law Firm
Gregory T. Genrich

Mr. McKean and Mr. Genrich described their experience in handling sales and transfers of restaurant permits. Mr. McKean and Mr. Genrich made the following points:

- Mr. McKean said that each municipality's quota is unique and based upon its population. Indianapolis' quota area is the boundaries of the old fire district.
- Mr. McKean said that demand for permits increases with population and the clustering of businesses.
- Mr. Genrich said that the timing of a transaction affects permit price. A buyer with a three year window for obtaining a permit will get a lower price than a buyer who needs one right away. Permit prices are also very location specific.
- Mr. McKean said that permits cannot be purchased and held for speculative purposes. If a permit holder can't begin the business operation immediately, the permit may be deposited with the alcohol and tobacco commission (ATC) for up to five years. Permits that are not purchased at auction must specify a location before the permit may be purchased.
- Mr. McKean said that he only has anecdotal evidence as to the effect that issuing additional permits has on the value of existing permits. When Carmel's population increased, the city received 11 new permits under the quota. Before the new permits were issued, permits sold for up to \$200,000; afterwards, permits sold for up to \$2,000.
- Mr. Genrich said that it is difficult to value a restaurant permit that is sold with a business because the value is tied in with the business' goodwill.

The LSA attorney, Anne Haley, distributed materials to the members regarding the quota systems of other states and the efforts of other states in dealing with issuing additional restaurant permits outside a quota (Exhibit 1).

The three tier system/direct wine shipping

Anne Haley, LSA attorney, read the charge to the Committee from House Enrolled Act 1118 (2008) regarding Indiana's three tier system: "The historic origins of Indiana alcoholic beverage laws and the Twenty-first Amendment to the Constitution of the United States and its place and purpose in the twenty-first century." Sen. Alting said that the Committee would take testimony on the issue of the three tier system and direct wine shipping in Indiana.

Marc Carmichael, Indiana Beverage Alliance

Mr. Marc Carmichael said that he represents beer wholesalers. Mr. Carmichael gave the Committee a written copy of his testimony (Exhibit 2). Mr. Carmichael made the following points:

- Each state has a unique set of alcoholic beverage laws because the 21st Amendment allows each state to adopt laws that reflect the will of their constituency.
- Before Prohibition, suppliers coerced retailers into selling their products and some suppliers also acted as retailers. After Prohibition, the wholesaler tier was created to separate the supplier and the retailer. Wholesalers regulate sales by ensuring retailers are licensed, preventing coercion of retailers, and collecting excise taxes.
- Polls of registered voters commissioned by the Indiana Beverage Alliance show that Indiana has a conservative view toward alcohol policy, indicating that a majority believe the primary role of the state is to ensure responsible consumption and that selling alcohol over the Internet would increase underage drinking.

Jim Purucker, Wine and Spirit Wholesalers of Indiana

Mr. Purucker made the following points:

- All states have some form of the three tier system. Thirty-two states use a licensed wholesaler for the middle tier, while in "control states", the state is the wholesaler. Wholesalers serve as an extension of the state by collecting excise taxes and ensuring that alcohol is sold to licensed retailers and dealers.
- Indiana already helps in-state wineries: (1)The Indiana wine grape market development fund receives a portion of the excise tax on wine. (2)The legislature increased the amount a winery can produce and still be considered a farm winery. (3)The law was changed to allow farm wineries to use out of state grapes and still be considered an Indiana product. (4)The legislature created a micro-wholesaler license and a direct wine seller's license.
- After the U.S. Supreme Court decision in *Granholm v. Heald (Granholm)*, the General Assembly amended the law to allow a compromise: in-state wineries could direct ship wine, but would no longer be able to sell directly to retailers.
- The state has invested \$7 million in the wine grape market development fund since its creation in 1979. Mr. Purucker questioned how good an investment this was since Indiana today has only 425 acres of wine grapes. In addition, there is some question as to whether the fund has been used for private purposes and federal lobbying.

Fred Biesecker, Ice Miller

Mr. Biesecker said that he would provide the Committee with a brief status report on the wine shipping litigation in Indiana and around the country. Mr. Biesecker said that he represented the ATC in the *Baude v. Heath (Baude)* litigation. Mr. Biesecker made the following points:

- *Granholm* involved a Michigan statute that expressly favored in-state wineries and a New York statute that subtly favored in-state wineries. The lessons learned as a result of *Granholm* were that the three tier system is legitimate and that in spite of the 21st Amendment, a state may not grant preferences to local wineries.
- Before *Granholm*, Indiana wineries could ship directly to consumers and retailers. After *Granholm*, the ATC stopped farm wineries from direct shipping. Furthermore,

the legislature eliminated two statutory provisions that conflicted with the *Granholm* decision: a provision that required a farm winery to produce wine from Indiana fruit and a provision requiring the holder of a farm winery permit to be a bona fide resident of Indiana for at least one year.

- In *Baude*, the U.S. District Court struck down as unconstitutional two provisions in the Indiana direct shipping law. One provision prohibited the holder of a direct wine seller permit from holding a wholesaler permit. The second provision required a consumer to provide the seller with identification and proof of age in an initial face-to-face transaction, before the consumer can have wine shipped directly by the seller. On appeal, the U.S. Court of Appeals for the 7th Circuit agreed with the District Court that the wholesaler provision is unconstitutional, but reversed the District Court as to the face-to-face provision, finding that the plaintiffs failed to prove their case on that issue. The court has indicated that the further away from the three tier system the law travels, the less likely the court will defer to the legislature's judgment. December 9 is the deadline for plaintiffs to file an appeal in *Baude* with the U.S. Supreme Court.
- There are two cases in the U.S. Court of Appeals for the 6th Circuit (from Kentucky and Tennessee) that bear watching because they involve the face to face requirement. If the decisions in these cases conflict with the 7th Circuit's decision in *Baude*, this may be one reason why the U.S. Supreme Court would decide to hear *Baude*.

Phil Terry, Monarch Beverage Company

Mr. Terry said that Monarch Beverage Company is a wine wholesaler. Mr. Terry made the following points:

- The three tier system is transparent and accountable. While suppliers in other industries have difficulty locating the source of defective or hazardous food products, alcoholic beverage manufacturers are able to quickly locate defective products through their wholesalers and in turn through their retailers.
- Wholesalers serve the state by collecting excise taxes and by selling the product only to licensed retailers or dealers.
- The law needs to strike a balance with regard to the availability of alcohol products. Restricting availability lowers consumption by minors at the risk of penalizing adults who want responsible access to alcohol.
- Some small batch wines produced by out of state wineries are not available to wholesalers because the supply is self-distributed by the winery or shipped directly to the consumer.

John Livengood, Indiana Association of Beverage Retailers/ Indiana Restaurant Association

Mr. Livengood said that he represents package liquor stores and the hospitality industry. He made the following points:

- The three tier system provides good service and price to retailers, so there is no need to "fix it".

- Package liquor stores were also created a result of the regulatory scheme after Prohibition to perform face to face sales of alcohol.
- Most large retailers do not want to distribute alcohol on their own, but if they do, prices for the smaller retailers will go up.
- Wholesalers are good corporate citizens that contribute to their communities.

David Heath, Chairman, Alcohol and Tobacco Commission

Chairman Heath said that the three tier system creates economic separation between the tiers, ensures an orderly market in the sale and distribution of alcohol, aids in the collection of excise taxes, and promotes moderate and legal alcohol consumption. Wholesalers are a necessary mechanism and the lowest cost means of regulation. Since the ATC has the power to sanction wholesalers, wholesalers have the incentive to regulate the retailers/dealers.

Lisa Hays Murray, Hays, Murray, Castor, LLC, Larry Satek, Satek Winery, Mark Easley, Easley Winery

Ms. Lisa Hays Murray gave a Powerpoint presentation regarding Indiana's wineries. A printed copy of that presentation is attached (Exhibit 3). Ms. Murray made the following points:

- In 2007, Indiana wineries produced 800,000 gallons of wine to make Indiana the tenth largest wine producer in the U.S. In 2008, Indiana has over 400 acres of vineyards. Indiana's 37 wineries collected \$400,000 in excise tax and \$2.8 million in sales tax.
- From 1971 until 2005, wineries could sell and ship directly to retailers and consumers in addition to selling wine in their tasting rooms. In 2005, wineries were prohibited from making direct shipments to Indiana consumers. In 2006, wineries were prohibited from selling directly to retailers and restricted to shipping only 3,000 cases to all Indiana customers. The law reduced shipping totals by at least 2/3, resulting in the closure of one winery and reducing Oliver Winery's shipments from approximately 2600 cases in 2004 to approximately 230 cases in 2008.
- There have been no access to minor violations for Indiana farm wineries for the last five years and states that have direct shipment have few, if any, problems. Only Indiana, Kansas, and Arizona have a face to face transaction provision in the law (Kentucky's was invalidated on appeal). Michigan, Ohio, and Georgia require electronic age verification. The state of Michigan, in adopting the electronic age verification requirement, said that the liability should not be on the wineries to collect and maintain copies of consumer's identification documents.
- Indiana retailers, dealers, and microbreweries can deliver directly to a consumer and there are no statutory safeguards in place to prevent minors from obtaining access to alcohol.
- Indiana wineries' 2009 legislative proposal is to: (1) provide third party verification as an alternative to the face to face requirement; (2) increase the direct seller shipping limit to 10,000 cases; (3) allow a farm winery permit holder to hold a 50% ownership interest in a micro-wholesaler permit; and (4) give wineries back their

wholesaler privileges by allowing them to sell not more than 2,000 gallons (833 cases) to retailers.

Larry Satek said that Indiana wineries' production decreased from 800,000 gallons in 2007 to 740,000 in 2008, affecting 20 to 30 jobs.

Mark Easley suggested that the legislature penalize delivery drivers for delivering alcohol to minors. Mr. Easley also suggested that alcohol education needs to be a part of the educational process, and said that lack of education causes people to binge when they reach 21 years old. Ms. Murray said that the U.S. Supreme Court in *Rowe v. New Hampshire Motor Transport*, which held that federal law preempts state regulation of common carriers, would probably prevent the state from legislating commercial drivers license penalties for common carrier drivers who deliver alcohol to minors.

John Keeler, Baker and Daniels, representing the Wine Institute

Mr. Keeler explained to the Committee that he represents the bigger, out of state wineries. Mr. Keeler made the following points:

- There is nothing wrong with the three tier system, but in the course of its 75 year existence there has been a growth of wineries and the number of citizens who enjoy wine legally and with moderation.
- The face-to-face requirement burdens Indiana and out of state wineries, because it requires consumers to travel to the wineries. He asked the Committee to look at the face to face requirement.
- Minors usually get alcohol from parents and friends, and by using fake IDs. Minors usually don't order a case of expensive wine and wait a week for it to arrive before they can drink it.
- With regard to collecting excise taxes on wine that is direct shipped, there is no proof that out of state wineries are scofflaws any more than in-state wineries.
- The three tier system works well for the sale of mass produced commodities like Gallo or Budweiser, but wine produced in limited quantities is difficult for the system to handle. There are over 40,000 wine labels produced today.

Vinsense, Inc.

Allen Dale Olson, President

Richard P. Hofstetter

Kenneth Harker, Jr.

Mr. Olson said that VinSense is a wine consumer advocacy group. Mr. Olson submitted his testimony to the Committee in writing (Exhibit 4). He also submitted a document entitled "Direct Wine Sales in Indiana: A Primer" (Exhibit 5) and a draft of legislation entitled "Direct Wine Sales Proposal" (Exhibit 6). The group made the following points:

- Mr. Olson said VinSense's goal is to enable Indiana consumers to purchase wine by electronic means from in-state and out of state producers and retailers. VinSense has no interest in eliminating wholesalers, but wants to eliminate the face to face requirement. The group supports preventing underage consumption of alcohol and the collection of all appropriate taxes.

- Mr. Hofstetter said that VinSense's proposal is to open up the market to 95% of the wineries that Indiana consumers can't purchase from because the wineries are too small. He said that other states allow or require electronic age verification for direct wine sales.
- Kenneth Harker, Jr. explained that Vinsense's proposal adds enough economic cost into the purchase of a direct shipped product that it is unlikely that it will supplant the mass marketing of the wholesaler. He said that some wineries produce 20 labels but only mass market 8 labels because the others are produced in such small quantities it is not cost effective.

3. Update of ATC implementation of alcohol server training

Sen. Alting said that Chairman Heath reported that implementation of alcohol server training would begin January of 2009.

4. Summary/discussion

Sen. Alting summarized the issues addressed by the Committee and asked for comments. With regard to additional restaurant permits in economic development areas, Sen. Alting said that the information presented to the Committee shows that developers don't object to paying the market price for restaurant permits. Sen. Alting said that he thinks the minimum bid for a permit should be the market price and the Committee needs to try to figure out how to determine that amount. With regard to displaying alcoholic beverages in separate areas of dealer establishments, the LSA attorney distributed to the Committee statutes and ordinances of states and local governments that require separate display of alcoholic beverages in grocery stores (Exhibit 7). With regard to Sunday sale of microbrewery products for carryout at Indiana microbreweries, Sen. Alting said that Sunday sales by microbreweries would be consistent with farm wineries' ability to make Sunday carryout sales. Rep. Bell said that he thinks microbreweries should be allowed Sunday carryout sales, limited to a half barrel per customer. Rep. Bell said that he supports creating a fund for microbreweries, similar to the Indiana wine grape market development fund for Indiana farm wineries. There were no other Committee comments.

Sen. Alting adjourned the Committee at 4:25 p.m.